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INFO RUEHBK/AMEMBASSY BANDAR SERI BEGAWAN 1298
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RUEHBJ/AMEMBASSY BEIJING 5129
RUEHHI/AMEMBASSY HANOI 3060
RUEHJA/AMEMBASSY JAKARTA 3846
RUEHKL/AMEMBASSY KUALA LUMPUR 3484
RUEHML/AMEMBASSY MANILA 9707
RUEHUL/AMEMBASSY SEOUL 7800
RUEHGP/AMEMBASSY SINGAPORE 6433
RUEHGZ/AMCONSUL GUANGZHOU 9276
RUEHHK/AMCONSUL HONG KONG 6332
RUEHGH/AMCONSUL SHANGHAI 0087
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RUEATRS/DEPT OF TREASURY WASHDC
RUCPDOC/DEPT OF COMMERCE WASHDC

C O N F I D E N T I A L SECTION 01 OF 03 TAIPEI 001462

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STATE PASS USTR
STATE FOR EAP/TC,
USTR FOR ALTBACH AND WINELAND,
USDOC FOR 4420/USFCS/OCEA/EAP/LDROKER
USDOC FOR 3132/USFCS/OIO/EAP/ADAVENPORT
USDOC FOR 4431/ITA/MAC/AP/OPB/TAIWAN/MBMORGAN
TREASURY ALSO PASS TO FEDERAL RESERVE/BOARD OF GOVERNORS,
AND SAN FRANCISCO FRB/TERESA CURRAN

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TAGS: EFIN ETRD ECON PREL TW

SUBJECT: TAIWAN FINANCE MINISTER TALKS ABOUT FINANCIAL REFORM

REF: A. TAIPEI 711
 1B. 05 TAIPEI 4178

Classified By: AIT Director Stephen M. Young for reasons 1.5 (b), (d)

11. (C) Summary: During an introductory call on April 21, Finance Minister Joseph Lyu and AIT Director Young discussed financial reform, Taiwan's efforts to be a regional financial center, the challenges of working with the opposition controlled Legislative Yuan (LY), and the overall economic health of the Taiwan economy. End summary.

12. (C) On April 21, 2006, AIT Director Young paid an initial courtesy call on Finance Minister Joseph Lyu (Jye-cherng). Mr. LIU Teng-cheng, Director General of the Department of the National Treasury, Mr. LIN Chi-chang, Director General of the Department of Taxation, and Ms. Joanne Ling, Secretary General of the Ministry of Finance (MOF) also attended the meeting.

Financial Reform Slows

13. (C) DIR Young asked about the pace of Taiwan's Second Stage of Financial Reform. Minister Lyu said that financial reform will continue, but "in a more cautious form." The number of government-owned banks will still be cut in half (from 12 to 6) through mergers, but the original plan to achieve this goal by December 2005 will probably not be realized until mid-2007.

14. (C) Lyu, the former chairman of BOT (Bank of Taiwan), said that BOT may not be privatized. He said that BOT has

special responsibilities, including being the sole distributor of Taiwan's currency, and implementing Taiwan's preferential interest rates for retired civil servants, which costs NT\$10 billion a year. Lyu believes that in these circumstances, it may be desirable for BOT to remain as the lone state-owned bank.

15. (C) Lyu said the executive branch wants to continue privatizing financial holding companies, but the Legislative Yuan (LY) is blocking this process by not allowing the further sale of government-owned shares. Lyu observed that LY members oppose selling government-owned shares in financial holding companies because there is a great deal of concern that the public will not benefit from the proposed mergers.

Taiwan as a Regional Financial Center?

16. (C) Asked about Taiwan's long-standing plans to become a regional financial services center, Lyu said that Taiwan needs to carefully assess its strengths. He said Taiwan will never be a New York, London or Tokyo in providing financial services, but he felt that Taiwan can find its own niche. He said that Taiwan is strong in manufacturing capability and can be a funding center for the region.

Budget Impasse

17. (C) The Director asked about the prospects for the LY to release funding under the central budget, noting that several

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agencies have told him their budgets remain frozen since January. Lyu pointed out some impending problems, such as that the Mainland Affairs Council only has funding until the end of April, but said he is optimistic that the funds originally frozen in January will be "defrosted." Lyu said that both parties need to be pragmatic and ask which priorities are in the national interest and which are open to debate, and then find common ground on issues that transcend partisan politics. He added that national defense and the special military need to be made a priority.

Credit Card Debt Not a Threat to Banking System

18. (C) Regarding the ongoing issue of "card slaves," (reflets) Lyu said the issue is a concern, but that it is a social rather than an economic concern. He said the situation does not present a threat to the banking system. Individuals need to take more responsibility for their actions, but some banks are also not being responsible in providing credit. He said that banks need to do a better job of reviewing credit histories before they issue cards. He added that the Financial Supervisory Commission (FSC) is responsible for regulating all bank operations and must take the lead on solving the card slave issue.

Economic Outlook

19. (C) The Director said that during meetings in both the private and public sector there seems to be a general level of pessimism about Taiwan's economic outlook. At the same time, he commented on the vitality he sees in the economy and wondered if this pessimism is overdone. Lyu agreed that some of the pessimism is due to psychological factors, but noted that Taiwan is likely to grow at 4% this year and for the next several. He said that while he would like to see higher growth, this is not a bad rate at all. He said that all of the dynamic economies in the region are pursuing improved capabilities in R&D, design, marketing and manufacturing. In his view, no single country can now accommodate all the stages of the value chains involved in producing and selling

goods. So Taiwan, like its neighbors, must determine where its comparative advantages lie in the value chains.

¶10. (C) Cross-strait relations play an important role in the future of the Taiwan economy, Lyu said, but the PRC is not the whole world. Taiwan businesses are very mobile and pragmatic. Minister Lyu recounted how one Taiwan businessman, an employer of tens of thousands of employees in the PRC, is already looking for the next manufacturing platform for the upcoming decades, and this might not be in the PRC.

COMMENT

¶11. (C) Lyu, Chen Sui-bian's first Finance minister with extensive international banking experience, faithfully stuck to the ruling party line on the range of issues. He supported passage of the special military budget, echoed recent comments by the Vice Premier about a slowing of the financial reform program and the Premier's comments to the Director that the card slave issue is more of a social issue than a threat to the banking system. End Comment.

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YOUNG